

**The Internal Revenue Service Can Improve Its
Reimbursable Program**

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INSPECTOR GENERAL
for TAX
ADMINISTRATION

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MEMORANDUM FOR COMMISSIONER ROSSOTTI

FROM: Lawrence W. Rogers /s/Lawrence W. Rogers
Acting Treasury Inspector General for Tax Administration

SUBJECT: Final Audit Report - The Internal Revenue Service Can Improve
Its Reimbursable Program

This report presents the results of our follow-up review of the Internal Revenue Service's (IRS) Reimbursable Program. We initiated this follow-up review to evaluate the effectiveness of the corrective actions taken in response to an Inspection Service Fiscal Year 1996 review of the Reimbursable Program.

In summary, corrective actions taken by the IRS have increased the accuracy of general ledger accounts related to the Reimbursable Program. These actions have also substantially reduced Accounts Receivable outstanding for Fiscal Years 1997 and 1998. Nevertheless, the IRS failed to complete certain recommended corrective actions, leaving the program susceptible to financial misstatements and uncollected accounts.

This report does not contain any new recommendations. However, we recommend that the National Director for Systems and Accounting Standards and the National Director for Financial Management complete the corrective actions planned in response to the prior report. These include implementing procedures to account correctly for Treasury Working Capital Fund Transactions, properly reconciling accounts using the Automated Financial System, and following up on overdue accounts receivable.

The National Director for Systems and Accounting Standards agreed with our recommendations and incorporated follow-up actions to ensure corrective actions are implemented timely. Management's comments have been incorporated into the report where appropriate and the full text of their comments is included as an Appendix.

Copies of this final report are being sent to Internal Revenue Service managers who are affected by the report recommendations. Please call me at (202) 622-6500 if you have any questions, or your staff may contact Maurice S. Moody, Acting Assistant Inspector General for Audit at (202) 622-8500.

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Corrective Actions Needed to Improve Its Reimbursable Program**

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Executive Summary

The Internal Revenue Service (IRS) Reimbursable Program manages a wide array of projects representing services which the IRS provides on a reimbursable basis to other entities such as states, foreign governments, and other federal agencies. Together, these reimbursable projects generated approximately \$90 million in annual revenues for Fiscal Year (FY) 1998.

The Treasury Inspector General for Tax Administration's Office of Audit (formerly Inspection Service Internal Audit) originally conducted a review of the Reimbursable Program in FY 1996. We initiated this follow-up review to evaluate the effectiveness of IRS management's corrective actions on the prior report.

Results

The National Director for Systems and Accounting Standards and the National Director for Financial Management had agreed to implement corrective actions in response to our prior report. Their completed corrective actions have helped increase operational efficiency and the collection of overdue accounts, and improve the accuracy of account balances. However, some of the planned corrective actions have been delayed or certified as complete when, in fact, they were not complete. This lack of follow-through increases the risk that financial statements will be inaccurate and that accounts will go uncollected.

Corrective Actions Completed

The New Reimbursable Revenue Posting Process Has Increased Operational Efficiency and Improved the Accuracy of Accounts

The Office of Financial Systems modified the process to record reimbursable revenue on the Automated Financial System (AFS) so that both proprietary and budgetary accounts are updated concurrently. As a result, staff time needed to post revenue transactions has been reduced by approximately 20 percent (\$20,000 in salary costs per year). Also, in contrast with the large discrepancies between the accounts in prior years (\$18.5 million in FY 1995 and \$28.7 million in April 1996), the FY 1997 proprietary and budgetary revenue accounts are now in agreement.

Reimbursable Accounts Receivable Have Been Substantially Reduced

Due to several changes implemented since the prior review, the Reimbursable Accounts Receivable is substantially lower. As of April 30, 1998, reimbursable accounts outstanding for FY 1997 totaled \$360,000. This is a significant reduction from the outstanding amounts of \$8 million for FY 1994 and \$16 million for FY 1995.

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Corrective Actions Not Completed

Procedures Have Not Been Developed to Account Correctly for Treasury Working Capital Fund transactions

The Office of Accounting Standards and Evaluation has not developed procedures to account correctly for Treasury Working Capital Fund (WCF) transactions. Because of this, IRS accounts are now manually adjusted using Treasury records at fiscal year end to reflect unexpended advances to the WCF. At the end of FY 1997, IRS recorded an adjustment of \$65 million using Treasury WCF records to reflect the funds advanced to the WCF and reduce recorded expenses. IRS still does not have the ability to reconcile its own records to Treasury WCF records. For example, as of June 17, 1998, AFS showed the Treasury WCF as owing the IRS \$12 million for telecommunications project services, while the Treasury WCF records showed that only \$4 million was owed to the IRS for these services.

Amounts Advanced to the IRS from Other Agencies Cannot be Recorded Properly on the Automated Financial System

The Office of Financial Systems did not take steps to make sure that AFS would accept advance transactions. AFS still does not allow input of advance transactions; therefore, advance payments are instead posted to a suspense account. While this suspense account reflected a balance of over \$7.5 million, IRS could not identify what portion of these amounts were advance payments.

The Unbilled Reimbursable Account and Reimbursable Receivable Account Are Not Properly Reconciled

The Office of Financial Systems issued updated Reimbursable Projects Accounting Procedures that require accounting technicians to maintain spreadsheets on each project rather than using AFS data to reconcile these accounts. No one reconciled the spreadsheet data to AFS accounts. As of March 1998, the FY 1993 through 1996 reimbursable accounts included approximately \$17 million of erroneous Accounts Receivable.

Procedures Do Not Require Follow-up Telephone Contacts on Overage Receivables

The updated Reimbursable Projects Accounting Procedures issued by the Office of Financial Systems do not require telephone contacts to account holders who do not respond to late notices. Follow-up telephone contacts should be used to keep accounts from becoming seriously delinquent. As of February 28, 1998, AFS reports reflected total Reimbursable Program Accounts Receivable of over \$33 million for FYs 1993 through 1998.

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Job Numbers Are Not Properly Used to Assist in the Automated Reconciliation of Reimbursable Project Accounts

The Office of Financial Systems did not modify AFS to require the use of job numbers on reimbursable transactions. Nine percent of the reimbursable receivable transactions were input without job numbers. Job numbers should be used to assist in the automated reconciliation of accounts by project.

Summary of Open Recommendations

This report makes no new recommendations. The National Director for Systems and Accounting Standards and the National Director for Financial Management should complete previously planned corrective actions that have been delayed or have not been fully implemented. These actions include:

- Developing and implementing procedures to account for, track and reconcile Treasury WCF transactions.
- Updating AFS to accept advance transactions.
- Updating procedures to require follow-up telephone contacts on overage receivables.
- Modifying AFS to require job numbers for reimbursable transactions and using AFS information to automate the account reconciliation process.

Management's Response

The National Director for Systems and Accounting Standards agreed with our findings and has committed to implement corrective actions on the open recommendations. He also included a follow-up plan to ensure the corrective actions are completed timely and are effective. His full response is included as Appendix V to this report.

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Objective and Scope

We conducted this follow-up review to determine the results of corrective actions taken in response to our report "Review of the IRS Reimbursable Program."

We initiated this follow-up review to determine the results of corrective actions taken in response to the Fiscal Year (FY) 1996 report titled *Review of the IRS Reimbursable Program* (Report Reference Number 066302). We performed tests in this follow-up review to determine whether corrective actions have achieved the following objectives:

- Revenue and expense transactions are recorded accurately.
- Accounts Receivable are posted in accordance with governmental accounting standards.
- Overdue Accounts Receivable are monitored, followed up on, and collected timely.

To determine whether these objectives have been achieved, we:

- Reviewed updated reimbursable project accounting procedures, transactions and related source documents to determine if revenues and expenses were recorded properly.
- Reviewed Accounts Receivable posting procedures, transactions, and reconciliations to determine if Accounts Receivable accurately reflected amounts owed to the Internal Revenue Service (IRS).
- Reviewed Accounts Receivable reports to determine the age of overdue accounts and reviewed a sample of reimbursable project files to determine actions taken to collect overdue amounts.

We conducted fieldwork at the Beckley Administrative Service Center from August 1997 through June 1998. Our review was conducted in accordance with generally accepted government auditing standards. Appendix I to this report contains the detailed objectives, scope and methodology of our review. A listing of major contributors to this report is shown in Appendix II.

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Background

IRS provides \$90 million worth of services to other entities on a reimbursable basis.

The IRS manages a wide array of reimbursable projects, which together generate annual revenues of approximately \$90 million. These projects represent services that the IRS provides on a reimbursable basis to other entities such as states, foreign governments, and other federal agencies.

The previous Internal Audit review identified several actions needed to improve controls and the accuracy of general ledger accounts for the IRS Reimbursable Program. In response to that review, IRS management agreed to correct the following problems:

- Accounting procedures were not adequate to properly record and reconcile Treasury Working Capital Fund (WCF) transactions.
- Reimbursable financial accounts differed significantly from budgetary accounts.
- Posting of transaction amounts to Accounts Receivable did not always follow federal financial accounting standards.
- The timeliness of collecting overdue accounts needed to be improved.

Appendix IV to this report lists the summary of recommendations and status of corrective actions from the prior review.

Results

IRS management has taken several corrective actions to improve financial management of the Reimbursable Program. However, more action is necessary to prevent problems from recurring.

IRS management has implemented several of the corrective actions needed to increase the accuracy of FY 1997 and 1998 general ledger accounts. As a result, IRS has substantially reduced Accounts Receivable outstanding for these years. However, management did not complete all of the agreed to corrective actions, thus increasing the risk that financial statements will be inaccurate and that accounts will go uncollected.

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Corrective Actions Completed

Management has taken several corrective actions since the prior review resulting in two major improvements.

- The new reimbursable revenue posting process has increased efficiency and the accuracy of accounts.
- Reimbursable Accounts Receivable have been substantially reduced.

The New Reimbursable Revenue Posting Process Has Increased Operational Efficiency and Improved the Accuracy of Accounts

An AFS modification has corrected the large discrepancies between reimbursable revenue accounts for financial accounting and the accounts used for budgeting.

Prior Condition

Reimbursable revenue accounts for financial accounting (proprietary accounts) did not agree with the accounts used for budgeting (budgetary accounts). There were differences between proprietary and budgetary revenue accounts of \$18.5 million in FY 1995 and \$28.7 million in April 1996. These discrepancies occurred because the transactions that affected these accounts needed to be input twice to the Automated Financial System (AFS). Consequently, mistakes occurred such as posting different amounts to the accounts or updating one account and not the other.

Planned Corrective Action

The National Director for Systems and Accounting Standards planned to have the Office of Financial Systems modify the process to record reimbursable revenue on AFS so that both proprietary and budgetary accounts are updated concurrently.

Follow-Up Results

The Office of Financial Systems has implemented the new process to record reimbursable revenue on AFS. This has reduced the time required to post revenue and has eliminated discrepancies between the accounts.

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- Accounting technicians had been spending 20 percent of their time updating budgetary revenue accounts. Now that the budgetary and proprietary accounts are updated concurrently, the duplicate posting to budgetary accounts has been eliminated, which equates to approximately \$20,000 annually in funds that could be put to better use.
- The FY 1997 proprietary and budgetary revenue accounts are now in agreement. This is a marked change from the large discrepancies in prior years (\$18.5 million in FY 1995 and \$28.7 million in April 1996).

Reimbursable Accounts Receivable Have Been Substantially Reduced

Prior Condition

Reimbursable Accounts Receivable were overstated and not always timely collected. There were outstanding amounts of \$8 million for FY 1994 and \$16 million for FY 1995. Despite the significant amount of outstanding accounts, IRS made only limited efforts to resolve or collect these accounts.

Planned Corrective Action

To help reduce the number and amount of overage Accounts Receivable, the National Director for Systems and Accounting Standards planned to implement the Accounts Receivable module in AFS to automate account follow-up.

Follow-Up Results

Outstanding Reimbursable Accounts Receivable were significantly lower for FY 1997 than for the years covered in the prior review, FYs 1994 and 1995. As of April 30, 1998, there were 74 reimbursable accounts outstanding for FY 1997 totaling \$360,000. This is a significant reduction from the outstanding amounts of \$8 million for FY 1994 and \$16 million for FY 1995. This reduction is primarily attributable to three factors:

Management's corrective actions have significantly reduced Accounts Receivable for FY 1997, as compared to prior years.

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- The implementation of the AFS Accounts Receivable module, which includes a system to send late notices automatically to agencies requesting payment of overdue amounts.
- The increased collection of contract amounts in advance of providing services.
- The elimination or transfer to other agencies of certain reimbursable projects, which reduced the total dollar amount of reimbursable contracts by approximately 30 percent.

IRS has also collected over \$480,000 from customers we contacted in the prior review and has recently contracted with a vendor to perform additional work on resolving overdue accounts. Beckley Administrative Service Center (ASC) personnel advised us that this vendor has helped IRS reduce erroneous and overdue Accounts Receivable from prior fiscal years by \$24.3 million. As of December 15, 1998, the Beckley ASC did not have enough documentation available and had not entered all the information on AFS for us to confirm this amount.

Corrective Actions Not Completed

Certain corrective actions management reported as being complete still required further action.

Despite the above improvements, we identified continuing problems related to corrective actions that management has not fully implemented. Management reported some of these corrective actions as completed. This follow-up report makes no new recommendations but does recommend that management complete corrective actions agreed to in the prior report (see Appendix IV).

Management needs to address the following concerns in order to complete corrective actions previously identified. This will further improve the accuracy of general ledger accounts and ensure that problems with aging receivables do not reoccur.

- Procedures have not been developed to account correctly for Treasury WCF transactions.

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- Amounts advanced to IRS from other agencies cannot be recorded properly on the Automated Financial System.
- The Unbilled Reimbursable account and Reimbursable Receivable account are not properly reconciled.
- Procedures do not require follow-up telephone contacts on overage receivables.
- Job numbers are not properly used to assist in the automated reconciliation of reimbursable project accounts.

Procedures Have Not Been Developed to Account Correctly for Treasury Working Capital Fund Transactions

Agencies using certain Treasury telecommunications services advance funds to the Treasury WCF to pay for their portion of these services. Funds advanced to the WCF in excess of fiscal year needs are carried over to subsequent years. Because of this, it is important that agencies accurately track their WCF balances to ensure amounts are expensed in the proper period and that unexpended fund balances are recorded properly.

Prior Conditions

Our prior review reported that IRS was not properly accounting for its funds advanced to the WCF.

IRS had several problems accounting for WCF transactions, including the following:

- (1) IRS was immediately recording funds advanced to Treasury as expenses even though the expense had not been incurred.
- (2) IRS did not have the ability to compare its fund balance in the WCF with the balance reflected on Treasury's WCF financial status reports.

Planned Corrective Actions

The National Director for Systems and Accounting Standards planned to have the Office of Accounting Standards and Evaluation develop and implement WCF

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procedures for IRS once the Department of Treasury issued Department-wide procedures. Treasury issued these Department-wide procedures in October 1997.

Follow-Up Results

IRS still has not developed procedures to properly record and account for its funds advanced to the Treasury WCF.

The Office of Accounting Standards and Evaluation has not developed or implemented WCF procedures and has not corrected either of the above conditions. Because of the delay in developing WCF procedures, IRS does not record advance payments. These payments should be recorded as an asset until they are used. However, since IRS keeps no record of advance payments, IRS must totally rely on Treasury WCF records to adjust accounts manually at fiscal year end to reflect the proper amount of unexpended advance payments. At the end of FY 1997, IRS recorded an adjustment of \$65 million using Treasury WCF records to reflect its funds advanced to the WCF and to reduce recorded expenses.

Because of the way WCF transactions are recorded on AFS, IRS still does not have the ability to reconcile its own records to WCF records. As noted in the prior report, IRS should use fields in the AFS database to identify WCF transactions. An AFS vendor code could be used to identify WCF transactions and a job number could be used to identify the specific WCF project. Without identifying these transactions on AFS, IRS will not have the ability to reconcile its records with WCF records.

Not reconciling WCF accounts has led to significant discrepancies between IRS and Treasury Department records.

Additionally, IRS receivable accounts from FY 1996 and prior are significantly overstated due to improper accounting for IRS revenue from WCF telecommunications services that IRS provided to other Treasury Bureaus in prior years. Errors due to lack of reconciliations between the WCF and AFS are still significant. For example, as of June 17, 1998, AFS showed the Treasury WCF as owing the IRS \$12 million for telecommunications project services. However, the Treasury WCF records showed that only \$4 million was owed to the IRS for these services. The lack of timely reconciliations for prior years reduces IRS' ability to substantiate amounts billed to the WCF.

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**Amounts Advanced to IRS from Other Agencies
Cannot be Recorded Properly on the
Automated Financial System**

Prior Condition

Payments received from other agencies before the IRS could provide services were posted to the Reimbursable Accounts Receivable (asset) account rather than to a liability account. This caused the Accounts Receivables to be misstated and the liability to be omitted. We recommended that IRS establish an advance account to record these transactions properly.

Planned Corrective Action

The National Director for Systems and Accounting Standards planned to have the Office of Financial Systems issue updated reimbursable procedures to specify the use of an advance account when recording payments received before IRS provides services.

Follow-Up Results

AFS still does not allow input of advance transactions. Consequently, accounting technicians must post advance payments to a suspense account.

Although the Office of Financial Systems developed procedures to account properly for funds advanced to IRS, AFS does not allow the input of these transactions.

The suspense account used for these advance payments is also used for other transactions that cannot otherwise be posted. On a June 1998 report, this suspense account reflected a balance of over \$7.5 million. However, IRS could not identify what portion of this amount was advance payments.

Not having the ability to identify these liability amounts on AFS could lead to financial reporting errors or improperly retaining excess amounts that should be refunded to agencies when advance payments are in excess of services used. For example, approximately \$500,000 of the \$7.5 million had been in suspense for over one year as of June 1998.

The Beckley ASC notified the Office of Financial Systems about this AFS problem after the new Reimbursable Projects Accounting Procedures were

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received in June 1997. However, as of December 15, 1998, they had not acted to correct the problem.

The Unbilled Reimbursable Account and Reimbursable Receivable Account Are Not Properly Reconciled

Prior Condition

The AFS reimbursable accounts contained overstated unbilled and billed Accounts Receivable. The 1996 report recommended that reviews of the billed and unbilled receivable accounts be included in periodic Accounts Receivable reconciliations.

Planned Corrective Actions

The National Director for Systems and Accounting Standards, in coordination with the National Director for Financial Management, planned to take the following corrective actions to ensure AFS general ledger accounts are accurate:

- Assign responsibilities for quarterly reviews of billed and unbilled reimbursable accounts.
- Update reimbursable procedures to include guidelines for verifying and adjusting these accounts.
- Develop reports to monitor this process.

Follow-Up Results

Management has not implemented the above corrective actions. As of March 1998, the FY 1993 through 1996 reimbursable accounts included approximately \$17 million of erroneous Accounts Receivable. In addition, an AFS download provided to us showed that substantial unbilled Accounts Receivable were still reflected on the FY 1993 through 1996 accounts.

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Accounting technicians are keeping duplicate manual records rather than using AFS information to reconcile accounts by project.

The May 1997 updated Reimbursable Projects Accounts Procedures require the accounting technicians to maintain spreadsheets on each project, rather than using the AFS system to reconcile these accounts. These spreadsheets are required so technicians can reconcile unbilled receivables to billed receivables and billed receivables to payments received for each project. AFS has the same billing and revenue data that is being manually input into the spreadsheets.

Keeping separate records on spreadsheets is an inefficient use of IRS resources. While it may have been helpful as a backup when AFS was first implemented, there should be no need to continue spending resources to maintain a separate and duplicate set of records. The maintenance of two separate systems allows for variances between systems, particularly since no one is reconciling the spreadsheet data to AFS accounts.

Maintenance of duplicate manual records is inefficient and it unnecessarily uses time needed for Accounts Receivable follow up.

The maintenance of duplicate records uses staff resources needed for Accounts Receivable follow-up. Accounting technicians estimated that they spend approximately 800 hours per year to maintain the separate spreadsheet data. Because the accounting technicians do not have time to follow up on overage receivables, the Beckley ASC contracted with a vendor to follow up on prior years' receivables. Over 50 percent of the \$72,000 vendor contract cost is allocable to the Reimbursable Program Accounts Receivable.

Procedures Do Not Require Follow-up Telephone Contacts on Overage Receivables

Prior Condition

Despite significant overage Accounts Receivable, IRS made no telephone contacts to determine whether these amounts were collectable. We selected a sample of 20 accounts to determine whether these amounts were collectable. Our contacts resulted in the collection of over \$480,000 in past due accounts from 17 of the 20 customers contacted. We recommended that procedures

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require telephone calls at specific periods to resolve overage Accounts Receivable.

Planned Corrective Action

To reduce overage Accounts Receivable, the National Director for Systems and Accounting Standards planned to have the Office of Financial Systems issue updated reimbursable procedures for following up on overage accounts.

Follow-Up Results

The updated Reimbursable Projects Accounting Procedures do not require telephone follow-up contacts. Supplemental guidelines only state that follow-up telephone calls are an option. Accounting technicians we interviewed stated that they are not making follow-up telephone contacts to overdue accounts on a regular basis due to other work priorities.

Even though IRS hired a vendor to make telephone contacts to clean up Accounts Receivable from prior years, its own procedures still do not require telephone contacts to delinquent accounts.

As of February 28, 1998, AFS reports reflected total Reimbursable Program Accounts Receivable of over \$33 million for FYs 1993 through 1998. We reviewed over 60 documents for accounts prior to 1997 and found that accounting technicians had not initiated any telephone follow-up contacts with customers since the 1996 review. In May of 1998, the Beckley ASC contracted with a vendor to follow up on overage receivables from years before 1997. We found that the vendor was following up by telephone to resolve old receivable amounts.

As noted previously, several other factors have helped to reduce the number and dollar amount of overage Accounts Receivable for FY 1997 and 1998. However, since the procedures do not require telephone contacts and technicians do not follow up on overage receivables, a control weakness remains, leaving the potential for future problems with overage receivables.

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Job Numbers are not Properly Used to Assist in the Automated Reconciliation of Reimbursable Project Accounts

Prior Condition

Accounting technicians did not consistently use reimbursable project or "job" numbers when posting reimbursable transactions on AFS. The 1996 report recommended requiring a job number for each reimbursable AFS transaction to help in reconciliations of billed, unbilled and Treasury WCF accounts.

Planned Corrective Action

The National Director for Systems and Accounting Standards planned to have the Office of Financial Systems analyze the impact of modifying AFS to require a job number for reimbursable transactions, and to make the change if appropriate. In addition, the Division planned to update procedures to require the use of job numbers whenever reimbursable transactions are posted.

Follow-Up Results

Although the updated Reimbursable Project Accounting Procedures require the use of a project number, AFS still does not require a valid job number to process Reimbursable Program transactions.

Although job numbers are needed to help reconcile reimbursable accounts by project, approximately nine percent of the reimbursable receivable transactions were input without a job number.

Approximately nine percent of the FY 1997 Reimbursable Accounts Receivable transactions were input without a job number. One of the primary benefits of this field in the AFS database is to identify the project to which a transaction belongs. The job number should be used to assist in the automated reconciliation of accounts by project. As previously noted, accounting technicians now use manual spreadsheets to reconcile billed and unbilled receivable amounts and payments for each project. Management should automate this process to allow use of an AFS query or report as previously planned.

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Recommendations:

The National Director for Systems and Accounting Standards in coordination with the National Director for Financial Management should take action to complete the following corrective actions that have been delayed or not fully implemented.

1. Develop and implement procedures to account correctly for WCF transactions.
2. Develop and implement procedures to track and reconcile WCF accounts for each WCF project.
3. Update AFS to accept advance transactions.
4. Provide accounting technicians instructions to reconcile Unbilled Reimbursable accounts and Reimbursable Receivable accounts using AFS rather than duplicate manual records. Automate the reconciliation process by use of queries and reports.
5. Update procedures to require follow-up telephone contacts on overage receivables.
6. Modify AFS to require job numbers for reimbursable transactions so that AFS information can be used to reconcile accounts by project.

Management's Response:

Management agreed with our report and plans to take the following corrective actions:

1. Procedures will be implemented to correctly account for WCF transactions and will require use of advance payment transactions on the AFS.
2. The vendor code field in the AFS will be used to track and reconcile WCF accounts and projects by establishing a vendor code for each project.
3. AFS has been corrected to accept advance payment transactions.
4. Procedures will be revised to provide instructions for reconciling reimbursable accounts using AFS rather than spreadsheets. AFS will be modified to generate an automated reconciliation report which will list

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revenues, billings and collections posted in AFS for each reimbursable project.

5. Procedures will be revised to require follow-up telephone contacts after the third late notice (90 days) and before the fourth late notice (120 days) if collection has not occurred.
6. So that the project number is consistently entered on all transactions, AFS will be modified to require document referencing, which will automatically include the project number.

Management has also included a follow-up plan to ensure the corrective actions are completed timely and are effective.

Conclusion

Our follow-up review found improvements based on corrective actions management has taken on recommendations in the 1996 report titled, *Review of the IRS Reimbursable Program*. The new reimbursable revenue posting process has increased efficiency and the accuracy of accounts. In addition, Reimbursable Accounts Receivable have been substantially reduced.

Although the IRS has implemented some of the recommended actions, further actions are needed to ensure accounts are accurate and collected timely.

However, management has not completed some of the recommended corrective actions they certified as complete. Management needs to take further action to correctly account for Treasury WCF transactions, properly record advances from other agencies, reconcile Accounts Receivable, and ensure overdue accounts are contacted by telephone. The lack of adequate corrective action in these areas increases the risk that financial statements will be inaccurate and that accounts will go uncollected.

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Appendix I

Detailed Objectives, Scope and Methodology

Our audit objectives were to determine the status of the corrective actions outlined in the Treasury Inventory Tracking and Closure (ITC) system for the Internal Revenue Service (IRS) Reimbursable Program and to determine whether the actions taken have corrected the conditions reported. To accomplish our objectives, we reviewed updated procedures, interviewed personnel responsible for Reimbursable Program operations and tested the Automated Financial System (AFS).

I. Implementation of Corrective Actions

To determine whether corrective actions have been implemented as reported to Treasury, we performed the following tests.

- A. We reviewed updated Treasury Department and IRS Reimbursable Program procedures to determine whether updated procedures have been established to:
 - 1. Properly account for Working Capital Fund (WCF) revenue and expense transactions.
 - 2. Require periodic reconciliations of the AFS fund balances to those on WCF reports.
 - 3. Require only one input to update associated reimbursable budgetary and proprietary accounts.
 - 4. Require direct posting of cash to revenues for projects which collect amounts as services are provided.
 - 5. Properly account for advance payments received from other agencies.
 - 6. Require reconciliations of the billed and unbilled receivables.
 - 7. Require follow-up telephone contacts on overage receivables.
 - 8. Require the use of job numbers on reimbursable project transactions.
- B. We interviewed employees responsible for Reimbursable Program transactions in order to determine whether they are following the updated procedures listed above.

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II. Effectiveness of Corrective Actions

In order to determine the effectiveness of corrective actions, we performed the following tests.

- A. To test the effectiveness of corrective actions taken to link budgetary and proprietary accounts, we:
 - 1. Reviewed AFS reports to document whether revenue and expense transaction codes update the proper budgetary and proprietary accounts.
 - 2. Interviewed the employees responsible for posting revenue and expense transactions to determine what steps they are taking.
 - 3. Analyzed the Fiscal Year (FY) 1997 AFS budgetary and proprietary revenue and expense accounts to determine whether these accounts are in agreement.
 - 4. Evaluated the cost savings of the new reimbursable revenue posting process by using an estimate of the staff time saved provided by the reimbursable analyst and accounting technicians. We estimated the value of this time by using an average of the accounting technician's salaries and benefits.
- B. To determine the effectiveness of corrective actions taken to improve the accuracy of Accounts Receivable, we:
 - 1. Interviewed employees responsible for billing and payment posting for projects that collect amounts as services are provided and reviewed billing and payment records to determine if actions were being taken timely.
 - 2. Interviewed employees responsible for advance payment postings and tested inputs of advance transactions to AFS to determine if the transactions were posting properly.
 - 3. Interviewed the senior Reimbursable Program analyst and accounting technicians to determine whether reconciliations of billed and unbilled receivables were being prepared.
 - 4. Reviewed an AFS download to determine if unbilled receivables were still reflected on FY 1994 through 1997 accounts.
 - 5. Interviewed the accounting technicians to determine whether they are following up on aging receivables with periodic telephone calls.
 - 6. Reviewed the aging receivables reports to determine the effectiveness of follow-up actions. We reviewed all 63 project files with overage accounts in excess of \$1,000 from FY 1993 through 1997 to determine if the records reflected timely follow-up actions and collections.
 - 7. Entered test AFS transactions to determine if the system required the entry of valid job numbers for reimbursable transactions.

**The Internal Revenue Service Has Not Taken All Required
Corrective Actions Needed to Improve Its Reimbursable Program**

Appendix II

Major Contributors to This Report

Stephen Mullins, Regional Inspector General for Audit (Western Region)

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**The Internal Revenue Service Has Not Taken All Required
Corrective Actions Needed to Improve Its Reimbursable Program**

Appendix III

Report Distribution List

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**The Internal Revenue Service Has Not Taken All Required
Corrective Actions Needed to Improve Its Reimbursable Program**

Appendix IV

**Summary of Recommendations and Status of
Corrective Actions (as of July 23, 1998)**

Recommendation	Internal Revenue Service Reported Status *	Further Action Needed?
Establish an advance account (asset) for Working Capital Fund (WCF) transactions.	COMPLETED (June 30, 1998)	Yes
Conduct periodic reconciliations between Automated Financial System (AFS) fund balances and those listed on the WCF financial status reports.	DELAYED (December 1, 1998)	Yes
Systemically link budgetary and financial accounts on AFS.	COMPLETED (November 30, 1996)	No
Reclassify reimbursement revenues from tax return photocopying to user fees.	REJECTED (January 1, 1997)	No
Directly post collections to revenue and cash accounts for projects which collect cash as services are provided.	COMPLETED (June 5, 1997)	No
Establish an advance account (liability) to record payments received before services are rendered.	COMPLETED (June 5, 1997)	Yes
Properly resolve all amounts in the Unbilled Reimbursable account.	COMPLETED (June 5, 1997)	Yes
Make periodic telephone calls to resolve overdue accounts.	COMPLETED (May 30, 1997)	Yes
Associate a job number with each reimbursable transaction that is processed through AFS.	COMPLETED (June 5, 1997)	Yes

** Source: July 23, 1998 Inventory, Tracking and Closure System report*

**The Internal Revenue Service Has Not Taken All Required
Corrective Actions Needed to Improve Its Reimbursable Program**

Appendix V

Management's Response to the Draft Report

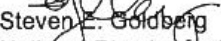


DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

February 22, 1999



MEMORANDUM FOR LAWRENCE W. ROGERS
ACTING TREASURY INSPECTOR GENERAL FOR
TAX ADMINISTRATION

FROM: 
Steven E. Goldberg
National Director for Systems and Accounting Standards

SUBJECT: Draft Internal Audit Report - "IRS Has Not Taken All Required
Corrective Actions Needed to Improve Its Reimbursable
Program"

Many improvements have been made to the Internal Revenue Service's (IRS) Reimbursable Program based on corrective actions taken since Internal Audit's prior review. The new reimbursable earnings posting process has increased efficiency and the accuracy of accounts, and accounts receivable have been substantially reduced. However, as indicated in your report, not all planned corrective actions were completed.

The following narrative addresses Internal Audit's recommendations and results identified during their follow-up review and our planned corrective actions.

1. IDENTIFICATION OF FINDING:

Procedures have not been developed to account correctly for Treasury Working Capital Fund (WCF) transactions.

RECOMMENDATION (1-1):

Develop and implement procedures to account correctly for WCF transactions.

ASSESSMENT OF CAUSE:

An advance payment transaction covering WCF exists in the Automated Financial System (AFS); however, we were awaiting issuance of Treasury's Department-wide procedures which were dated November 4, 1998, prior to issuing IRS procedures. Subsequent to receiving this draft internal audit report, we were informed by TIGTA that Treasury issued procedures in October 1997. These procedures were faxed to us upon request.

The Internal Revenue Service Has Not Taken All Required Corrective Actions Needed to Improve Its Reimbursable Program

CORRECTIVE ACTION:

Policy and procedures will be implemented to correctly account for WCF transactions and require use of the advance payment transaction in AFS.

PROPOSED IMPLEMENTATION DATE:

May 1, 1999

RESPONSIBLE MANAGEMENT OFFICIAL:

National Director for Systems and Accounting Standards

CORRECTIVE ACTION MONITORING PLAN:

The Working Capital Fund advance account will be monitored quarterly by the Systems and Accounting Standards Division for one year to determine compliance with policy and procedures. The results will be documented and kept on file.

RECOMMENDATION (1-2)

Develop and implement procedures to track and reconcile WCF accounts for each WCF project.

ASSESSMENT OF CAUSE:

Awaiting issuance of Treasury's Department-wide procedures which were dated November 4, 1998, prior to issuing IRS procedures. Subsequent to receiving this draft internal audit report, we were informed by TIGTA that Treasury issued procedures in October 1997. These procedures were faxed to us upon request.

CORRECTIVE ACTION:

Procedures will be implemented to reconcile WCF accounts in AFS against Treasury's WCF financial status report for each WCF project. The vendor code field will be used to track and reconcile WCF accounts and projects by establishing a vendor code for each project. Reports will be created listing vendor code/project and transaction information for use in the reconciliation process. The vendor code field is a more reliable way to track projects since use of the job number field in AFS is only mandatory for the Information Systems appropriation.

**The Internal Revenue Service Has Not Taken All Required
Corrective Actions Needed to Improve Its Reimbursable Program**

DATE PLANNED TO BE COMPLETED:

May 1, 1999

RESPONSIBLE MANAGEMENT OFFICIAL:

National Director for Systems and Accounting Standards

CORRECTIVE ACTION MONITORING PLAN:

Working Capital Fund transactions will be reviewed quarterly by the Systems and Accounting Standards Division for one year to determine compliance with using the vendor code to identify and track projects. In addition, the procedures will instruct the Beckley Administrative Services Center to submit a quarterly report on reconciliation to the Systems and Accounting Standards Division for review of report information with account information. These actions will assist in determining whether policy and procedures are being followed and/or whether deficiencies are still present. The results will be documented and kept on file.

2. IDENTIFICATION OF FINDING:

Amounts advanced to IRS from other agencies cannot be recorded properly in AFS.

RECOMMENDATION (2-1):

Update AFS to accept advance transactions.

ASSESSMENT OF CAUSE:

Updated Reimbursable procedures were issued and AFS was updated with transactions to record advances to standard general ledger account 2310, Advances from Others, and deposit fund account 6734, Deposit of Collections-Reimbursable Services. However, a problem was encountered when using these transactions and another AFS transaction was used.

CORRECTIVE ACTION:

These transactions have been reviewed and corrected to eliminate this problem and guidance will be issued instructing accounting operations to properly record the advances.

The Internal Revenue Service Has Not Taken All Required Corrective Actions Needed to Improve Its Reimbursable Program

DATE PLANNED TO BE COMPLETED:

May 1, 1999

RESPONSIBLE MANAGEMENT OFFICIAL:

National Director for Systems and Accounting Standards

CORRECTIVE ACTION MONITORING PLAN:

The advance account will be reviewed on a quarterly basis by the Systems and Accounting Standards Division for one year to determine whether advances are being recorded correctly. The results will be documented and kept on file. In addition, a financial operations bulletin board will be implemented to allow users to report, among other issues, problems with transaction processing in AFS. Problems and issues reported will be monitored to ensure resolution.

3. IDENTIFICATION OF FINDING:

The AFS Unbilled Reimbursable accounts and Reimbursable Receivable accounts are not properly reconciled.

RECOMMENDATION (3-1):

Provide accounting technicians instructions needed to reconcile Unbilled Reimbursable accounts and Reimbursable Receivable accounts using AFS rather than keeping duplicate manual records.

ASSESSMENT OF CAUSE:

Funding for modifications to AFS was questionable during fiscal year 1998 due to the Y2k enhancement. Therefore, procedures suggested an alternate method for reconciling Unbilled Reimbursable accounts with Reimbursable Receivable accounts.

CORRECTIVE ACTION:

The Reimbursable procedures will be revised to remove the suggested use of a spreadsheet and to provide instructions for reconciling Unbilled Reimbursable accounts and Reimbursable Receivable accounts using AFS and an automated report.

DATE PLANNED TO BE COMPLETED:

August 1, 1999

The Internal Revenue Service Has Not Taken All Required Corrective Actions Needed to Improve Its Reimbursable Program

RESPONSIBLE MANAGEMENT OFFICIAL:

National Director for Systems and Accounting Standards

CORRECTIVE ACTION MONITORING PLAN:

Reimbursable Receivable accounts will be monitored on a quarterly basis by the Systems and Accounting Standards Division for one year to determine compliance with revised procedures. In addition, an operational review will be conducted to physically review randomly selected projects. The results will be documented and kept on file.

RECOMMENDATION (3-2):

Automate the reconciliation process by use of queries and reports.

ASSESSMENT OF CAUSE:

Funding for modifications to AFS was questionable during fiscal year 1998 due to the Y2k enhancement. Therefore, procedures suggested an alternate method for reconciling Unbilled Reimbursable accounts with Reimbursable Receivable accounts.

CORRECTIVE ACTION:

AFS will be modified to require the billing document to reference the earnings document which will aid in the reconciliation process as well as bring all documents relating to a specific reimbursable billing onto another existing table in AFS. This referencing requirement will also provide the ability to create an automated reconciliation report which will list earnings, billings and collections posted in AFS for each reimbursable project.

DATE PLANNED TO BE COMPLETED:

August 1, 1999

RESPONSIBLE MANAGEMENT OFFICIAL:

National Director for Systems and Accounting Standards

CORRECTIVE ACTION MONITORING PLAN:

Reimbursable Receivable accounts will be monitored on a quarterly basis by the Systems and Accounting Standards Division for one year to determine compliance with revised procedures. In addition, an operational review will be conducted to physically

The Internal Revenue Service Has Not Taken All Required Corrective Actions Needed to Improve Its Reimbursable Program

review randomly selected projects. The results will be documented and kept on file.

4. IDENTIFICATION OF FINDING:

Procedures do not require follow-up telephone contacts on overage receivables.

RECOMMENDATION (4-1):

Update procedures to require follow-up telephone contacts on overage receivables.

ASSESSMENT OF CAUSE:

Previous planned corrective actions were completed as stated. The initial planned corrective actions did not specify that there would be required telephone follow-ups on overaged receivables.

CORRECTIVE ACTION:

The procedures will be revised to require follow-up telephone contacts after the third dunning notice (90 days) and prior to the fourth dunning notice (120 days) if collection has not occurred.

DATE PLANNED TO BE COMPLETED:

August 1, 1999

RESPONSIBLE MANAGEMENT OFFICIAL:

National Director for Systems and Accounting Standards

CORRECTIVE ACTION MONITORING PLAN:

Reimbursable Receivable accounts will be monitored quarterly by the Systems and Accounting Standards Division for one year to ensure telephone follow-up is taking place. The results will be documented and kept on file.

5. IDENTIFICATION OF FINDING:

Job numbers are not properly used to assist in automated reconciliation of reimbursable project accounts.

The Internal Revenue Service Has Not Taken All Required Corrective Actions Needed to Improve Its Reimbursable Program

RECOMMENDATION (5-1):

Modify AFS to require job numbers for reimbursable transactions so that AFS information can be used to reconcile accounts by project.

ASSESSMENT OF CAUSE:

Under current system constraints the job number field in AFS can only be required for the Information Systems appropriation. System and procedural analysis concluded that using the job number field to enter project numbers is a major enhancement, both procedurally and systemically. Funding is not available for such a major modification to AFS at this time.

CORRECTIVE ACTION:

The Reimbursable Project Accounting Procedures currently require use of a project number when posting reimbursable transactions. The project number is a part of the management activity code (MAC). AFS will require the project number be entered in the job number field only when the project posts to the Information Systems appropriation. However, so that the project number is consistently entered on all transactions affecting a specific earning document, AFS will be modified to require document referencing which will automatically pull the entire accounting string, including the project number, to the referenced document.

DATE PLANNED TO BE COMPLETED:

August 1, 1999

RESPONSIBLE MANAGEMENT OFFICIAL:

National Director for Systems and Accounting Standards

CORRECTIVE ACTION MONITORING PLAN:

System testing will be performed by the Systems and Accounting Standards Division prior to implementing the referencing modification in AFS.

If you have any questions or require further information, feel free to contact me at (301) 492-5400, extension 320 or have a member of your staff contact Serva Borum, Acting Chief, Office of Financial Systems, on extension 310.

cc: Chief Financial Officer
National Director for Financial Management